In the Supreme Court of the United States

OCTOBER TERM, 1965

No. 613

THE DANFORTH FOUNDATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

Section 101(6) of the Internal Revenue Code of 1939, 53 Stat. 33, as amended, 26 U.S.C. (1952 ed.) 101(6), provided that corporations organized and operated exclusively for religious, charitable and educational purposes were exempt from the income tax. Section 3814(1) of the Internal Revenue Code of 1939, as added by Section 331 of the Revenue Act of 1950, c. 994, 64 Stat. 906, 958, provided that, with respect to any such organization—

> if the amounts accumulated out of income during the taxable year or any prior taxable year and

not actually paid out by the end of the taxable year—

> (1) are unreasonable in amount or duration in order to carry out the charitable, educational, or other purpose or function constituting the basis for such organization's exemption under section 101(6) * * *,
>
> * * * *
>
> * * * exemption under section 101(6) shall be denied for the taxable year. [26 U.S.C. (1952 ed.) 3814].

The taxpayer Danforth Foundation is a charitable corporation which, according to its Articles of Incorporation, was "formed solely and only for purely charitable, educational and religious purposes and to promote the well-being of mankind throughout the United States" (Pet. App. 16). The Commissioner by letter dated April 13, 1939, advised the taxpayer that it was exempt from income tax under Section 101(6) for 1939 and "subsequent years so long as there is no change in your organization, your purposes or your method of operation" (Pet. App. 16).

The taxpayer received most of its assets as gifts from William H. Danforth and his wife; these consisted principally of stock of the Ralston Purina Company, of which Danforth had been president and then chairman of the board (Pet. App. 2, 22). The initial gift, made in 1927, was of assets worth approximately $100,000; the total value of such gifts was about $4,800,000 *(ibid.)*. The value of the taxpayer's assets has increased tremendously (Pet. App. 22). By 1950 they were worth approximately $24,000,000; ten

years later their value was more than $98,000,000 *(ibid.)*.

At the end of 1950, the taxpayer's accumulated income, less capital gains, was $4,311,689. For the years 1951 and 1952 its gross income, less capital gains, was $1,290,241 and $1,221,295, respectively. In the same years, its respective charitable expenditures were $128,284 and $176,181, constituting approximately 10 percent and 14 percent of its gross income in those years. During those two years taxpayer increased its accumulated gross income by more than $2,000,000, to $6,394,739 at the end of 1952 (Pet. App. 22, 14).[1]

Throughout the years the taxpayer's principal activity was the sponsorship and support of leadership training programs designed to encourage religious and spiritual impulses (Pet. App. 8-9). In 1945 taxpayer's trustees began to look for a fulltime director of the Foundation (Pet. App. 9). They decided upon a college president who, because of his prior commitments, delayed deciding whether to accept the post until 1949, when he agreed to become the director on January 1, 1951 (Pet. App. 9-10). Upon taking office the new director proposed various programs to the trustees, and preliminary steps looking toward the inauguration of such programs were taken in 1951 and 1952 (Pet. App. 10-11).

In 1958, the Commissioner advised the taxpayer that he had determined that the accumulation of in-

---

[1] A table, showing the taxpayer's assets, income and accumulations for the years 1944 through 1952, appears in the opinion of the district court (Pet. App. 7).

come for the years 1951 and 1952 was unreasonable under Section 3814, and that he was modifying his 1939 ruling to the extent of disallowing exemption from income taxes for those years (Pet. App. 1, 17). The taxpayer paid the taxes thus assessed, and then brought suit for refund in the district court. The court held for the government (Pet. App. 14). It ruled (Pet. App. 10, 12) that although "the trustees' decisions to accumulate income [in 1951 and 1952] were made in good faith and in anticipation of early formulation of expansive programs which they believed would more than use the accumulated funds,"

> nevertheless, the evidence presented fails to show that the programs adopted will, as budgeted, begin to use expected annual income, let alone that accumulated before the questioned period. Furthermore, the record is absent any showing of attempt to relate the programs to anticipated income. Expenditures for programs designed by the end of 1951 could not be expected to exceed $300,000.00 in charitable grants, and under all programs designed by the end of 1952, expenditures could not be expected to exceed $500,000.00 in the immediate future. Further projection of probable charitable grants under programs of the Foundation would require speculation. Meanwhile, subsequent annual income could reasonably be anticipated to exceed $1,000,000.00. The conclusion that the unexpended income of $1,104,990.98 in 1951 and $978,059.24 in 1952, making a total accumulation of $6,394,739.46 by the end of 1952, constitute unreasonable accumulations is inescapable. * * * [Pet. App. 14.]

The court of appeals affirmed. It held (Pet. App. 19-21, 25) that the district court had applied the correct test for determining whether accumulations of income are unreasonable under Section 101(6)—*i.e.*, whether the organization had a "concrete program for the accumulation of income which will be devoted to a charitable purpose and in the light of existing circumstances is the program a reasonable one?"; that it was "obvious that it would have taken the Foundation many years to devise well-conceived, self-operated programs [of the kind which it was sponsoring] which would consume its substantial and growing annual income" (Pet. App. 25); and that the trial court's finding that the taxpayer's accumulation of income in 1951 and 1952 was unreasonable was "adequately supported by substantial evidence" *(ibid.)*.

The holding of the court of appeals that accumulations of income by a charitable organization are unreasonable under Section 101(6) unless (1) they are made pursuant to a concrete program for their subsequent utilization and (2) their amount is reasonably appropriate to accomplish such specific program, accords with a prior decision of the same court which this Court refused to review and with the decision of the only other circuit that has decided the question. *Stevens Bros. Foundation, Inc.* v. *Commissioner*, 324 F. 2d 633 (C.A. 8), certiorari denied, 376 U.S. 969; *Erie Endowment* v. *United States*, 316 F. 2d 151 (C.A. 3). These are appropriate standards for determining whether an accumulation is unreasonable, since they effectuate the congressional purpose, re-

flected in the legislative history, "to force * * * charitable organizations to spend currently the money which they receive for the purposes upon which their favored tax status is based." 96 Cong. Rec. 14057, quoted by the court below, Pet. App. 19. When a charitable oganization accumulates most of its income but without a specific plan which such accumulations are designed to further, the accumulations are "unreasonable" under the statute because they are not geared to the accomplishment of any particular charitable objective. And, as the court of appeals pointed out (Pet. App. 24-25), "it is possible for a foundation to comply with the unreasonable income accumulation provision of § 3814 within a reasonably short time," since "[t]he trustees, after learning in 1953 that the income tax-exemption was being questioned by reason of income accumulations, rapidly increased the Foundation's non-program grants to qualified beneficiaries and thus made sufficient use of its income to entitle it to tax exemption for 1953 and subsequent years."

In the present case, petitioner does not—and plainly could not—challenge the district court's findings, which the court of appeals upheld as supported by substantial evidence, that the programs the Foundation had formulated by the end of 1952 fell far short of absorbing its reasonably anticipated income for those and subsequent years. The district court pointed out (Pet. App. 14) that "under all programs designed by the end of 1952, expenditures could not be expected to exceed $500,000.00 in the immediate

future," but that "subsequent annual income could reasonably be anticipated to exceed $1,000,000.00." In these circumstances the accumulation in 1951 and 1952 of $2,000,000 (representing 90 percent and 86 percent of gross income in those years, respectively), which increased the Foundation's total accrued accumulations to more than $6,000,000, plainly was unreasonable.

The petition for a writ of certiorari should be denied.

Respectfully submitted.

THURGOOD MARSHALL,
Solicitor General.

RICHARD M. ROBERTS,
Acting Assistant Attorney General.

MORTON K. ROTHSCHILD,
ROBERT A. BERNSTEIN,
Attorneys.

OCTOBER, 1965.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1965 791501 292

Office-Supreme Court, U.S.
FILED
NOV 4 1965
JOHN F. DAVIS, CLERK

No. 613

IN THE

Supreme Court of the United States

OCTOBER TERM, 1965

THE DANFORTH FOUNDATION,
Petitioner,

vs.

UNITED STATES OF AMERICA,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

PETITIONER'S REPLY MEMORANDUM

ALBERT E. JENNER, JR.
135 South La Salle Street
Chicago, Illinois 60603
Attorney for Petitioner

UNITED STATES LAW PRINTING CO., CHICAGO 18, ILL. LA review 5-6581

IN THE

Supreme Court of the United States

OCTOBER TERM, 1965

No. 613

THE DANFORTH FOUNDATION,

Petitioner,

VS.

UNITED STATES OF AMERICA,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

PETITIONER'S REPLY MEMORANDUM

The petition for writ of certiorari directs the Court's attention to the patently improper test applied to the facts of this case by the Court of Appeals for the Eighth Circuit. The government's memorandum in opposition emphasizes the use of that faulty test and illustrates its impropriety.

The government, with reference to the Court of Appeals opinion, states (Memorandum, p. 5):

> ". . . It held . . . that the district court had applied the correct test for determining whether accumulations of income are unreasonable under Section 101(6)—*i.e.*, whether the organization had a 'concrete program for the accumulation of income which will be devoted to a charitable purpose and in the light of existing circumstances is the program a reasonable one?' . . ."

As pointed out in the petition, this test is far out of line with the clear import of the statute. The legislative history does not contradict the unequivocal language of the statute, *viz.*, an accumulation must be *unreasonable* in order for an exemption to be denied. The "concrete program" test may be a short-cut solution to the difficult problem of determining reasonableness, but it is a short cut which, as in the instant case, could read the requirement of reasonableness out of the statute. It is a short-cut which could work a considerable injustice upon a charitable organization such as the Danforth Foundation which, in good faith, was beginning to plan extensive charitable endeavors.

Petitioner will suffer a grave injustice if certiorari is denied. The impropriety of the standards applied by the Court of Appeals was compounded by its error in applying the statute retroactively. (Petition, p. 10.) However, what is more important from this Court's point of view, is the fact that the lower courts are misinterpreting an act of Congress.* As the government points out (Memorandum,

---

* Section 3814, Internal Revenue Code of 1939, has, with minor revisions, become Section 504 of the Internal Revenue Code of 1954.

p. 5), the Court of Appeals in the instant case was following its decision in *Stevens Bros. Foundation, Inc.* v. *Commissioner*, 324 F. 2d 633 (8th Cir. 1963), *cert. denied*, 376 U.S. 969, and the decision of the Third Circuit in *Erie Endowment* v. *United States*, 316 F. 2d 151 (3d Cir. 1963). It would be appropriate at this time for this Court to correct the improper rulings of two of the circuits.

The petition for certiorari to the United States Court of Appeals for the Eighth Circuit should be granted.

Respectfully submitted,

ALBERT E. JENNER, JR.
135 South LaSalle Street
Chicago, Illinois 60603
RA 6-0220
Attorney for Petitioner

END